

The Honorable Richard A. Jones

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

In re

CHRISTINE TAVARES, and
EDWARD ANZALDUA,

Debtors,

MICHAEL KLEIN, Trustee for the
estate of Christine Tavares, and
DENNIS LEE BURMAN, Trustee for
the estate of Edward Anzaldua,

Plaintiff,

vs.

ALABAMA HOUSING FINANCE
AUTHORITY, a foreign public
corporation doing business in
Washington as SERVISOLUTIONS

Defendant

U.S. Dist. Ct. Appeal 2:19-cv-00020-RAJ

Adversary Case No. 18-01002-MLB

Chpt. 7 Bankruptcy Case No.s
16-14901-MLB
16-15970-MLB

Bankruptcy Internal Appeal 19-S001

APPELLANTS' REPLY BRIEF

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1 RCW 19.86.093

8, 10

2 **Miscellaneous:**

3 FRCP 15

14, 15

4 5 **I. INTRODUCTION**

6 The Respondent's responsive brief does not shed any light on any legitimate
7 justification for its total refusal to assist Ms. Tavares with affordable mitigation.

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9 Respondent, Alabama Housing Finance Authority ("AHFA") is taking advantage of
10 the fact that her former domestic partner, Mr. Anzaldua, also co-borrower on the note,
11 is withholding his income data in retaliation for Ms. Tavares reporting his sexual
12 assault and obtaining a No Contact Order (NCO) to protect her child from him.
13

14 15 **II. APPELLATE JURISDICTION**

16 The District Court has jurisdiction over this appeal. Dkt. No 6, pg. 6.
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19 **III. STANDARD OF REVIEW**

20 Bankruptcy Trustee Appellants stated the correct standard of review in their
21 opening brief. *In re Turner*, 859 F.3d 1145, 1148 (9th Cir. 2017). The Ninth Circuit
22 Court of Appeals also reviews district court decisions appealed from bankruptcy
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1 courts de novo. *Mano-Y & M, Ltd. v. Field (In re The Mortgage Store, Inc.)*, 773 F.3d
2 990, 994 (9th Cir. 2014).

3 A bankruptcy court's decision to deny leave to amend the complaint is reviewed
4 for abuse of discretion, however, whether the complaint is susceptible to amendment
5 is reviewed de novo. *Turner*, 859 F.3d at 1148; *Thinket Ink Info Res., Inc. v. Sun*
6 *Microsystems, Inc.*, 368 F.3d 1053, 1061 (9th Cir. 2004).
7

8 9 10 **IV. STATEMENT OF THE ISSUES**

11 1. Whether the bankruptcy court erred when it ruled that the adversary
12 complaint failed to state a claim?

13 2. Whether the bankruptcy court erred by denying the Bankruptcy Trustees leave
14 to amend the adversary complaint?
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18 **V. ARGUMENT**

19 20 **1. The bankruptcy court erred when it ruled that the adversary** 21 **complaint failed to state a claim.**

22 AHFA's denials (Dkt. No. 7, pg. 10 of Appellee's Brief) cover up the shell game
23 AHFA imposed on Ms. Tavares, (AHFA first informed Ms. Tavares that Mr. Anzaldúa
24 could execute a quitclaim deed because he no longer resided in the property.
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26

Adversary Proceeding Dkt. No. 7 at pg. 2, ¶11. Then AHFA switched positions and informed Ms. Tavares that a quitclaim would not help. Adversary Proceeding Dkt. No. 7, pg. 3, ¶13. Along with discouraging Ms. Tavares from using Legislatively promoted housing counselors (*See* Intent under RCW 61.24.005), AHFA's representations to Ms. Tavares then, as in its response now, attempts to deflect the issue with indecipherable denials regarding programs that Ms. Tavares's HUD-approved housing counselor (Patzner) declared Ms. Tavares would have qualified for. Adversary Proceeding Dkt. No. 27-7, pg. 3. None of AHFA's denials sufficiently provide the basis of the denial and as indicated by Ms. Tavares's housing counselor, it was based on incorrect income data. *Id* and Appellant's Opening Brief at pg. 12.

Washington's Supreme Court held that, "Washington's Deed of Trust Act should be construed to further three basic objectives. First, the nonjudicial foreclosure process should remain efficient and inexpensive. Second, the process should provide an adequate opportunity for interested parties to prevent wrongful foreclosure. Third, the process should promote the stability of land titles." *Bain v. Metro. Mortg. Grp., Inc.*, 175 Wn.2d 83, 93, 285 P.3d 34 (2012) citing *Cox v. Helenius*, 103 Wash.2d at 387, 693 P.2d 683 (2010). In furtherance of the above, and in the midst of the foreclosure crisis, Washington's Legislature amended its Deeds of Trusts Act ("DTA") with the Foreclosure Fairness Act ("FFA"), the substitute house bill described the amendment as an act relating to "protecting and assisting homeowners from

unnecessary foreclosure....” 2011 SHB 1363, Chpt. 58, 62nd Legis. The Legislatures findings and intent under RCW 61.24.005 clearly states its intentions to, “ Encourage homeowners to utilize the skills and professional judgment of housing counselors as early as possible in the foreclosure process and create a framework for homeowners and beneficiaries to communicate with each other to reach a resolution and avoid foreclosure whenever possible....” RCW 61.24.005 Findings-Intent-2001 c58, (2)(a) (b).

Hangman Ridge

Generally, to prevail in a private CPA claim, the plaintiff must prove (1) an unfair or deceptive act or practice (2) occurring in trade or commerce (3) affecting the public interest, (4) injury to a person's business or property, and (5) causation.

Hangman Ridge Training Stables. Inc . v. Safeco Title Ins. Co., 105 Wn.2d 778, 784-85, 719 P.2d 531 (1986). The bankruptcy court erred by modifying the *Hangman Ridge* analysis requiring that each alleged unfair of deceptive act, separately and individually must survive the *Hangman Ridge* analysis. This distorts each element’s context and ignores the cumulative effect of AHFA’s alleged unfair and deceptive acts as well as the Legislative Intent.

(1) an unfair or deceptive act or practice

Plaintiffs need not show that the act in question was intended to deceive, but that the alleged act had the capacity to deceive a substantial portion of the public.

1 *Hangman Ridge*, 105 Wn.2d 785. The "unfair or deceptive act" element can be
 2 established by alleging an act that has the capacity to deceive a substantial portion of
 3 the public, or by showing that AHFA's conduct violates a statute that contains a
 4 specific legislative declaration of public interest impact, or AHFA had the capacity to
 5 injure other persons, or AHFA has the capacity to injure other persons. RCW
 6 19.86.093(2) & (3). In contrast to the HUD-approved housing counselor's assertion
 7 that there was a modification Ms. Tavares could have independently qualified for,
 8 AHFA simply gives conclusory statements that Ms. Tavares did not qualify for a loan
 9 modification.
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12 Instead of communicating with Ms. Tavares or giving any credence to her
 13 housing counselor, AHFA's sent HUD an prejudicially biased variance request (Dkt 71-
 14 11) indicating Mr. Anzaldua's molestation as "alleged" but lacks no certainty in
 15 stating, "Mr. on note must provide inc for lm rvw per pg 599." Further clouding
 16 communication, AHFA vaguely asked HUD, "[D]oes HUD appr exclusion of co-brwr
 17 income and signature?" Without indicating which co-borrower the request was about
 18 nor did the request contain any income data that HUD could rely on in deciding the
 19 variance. Dkt. 71-11. AHFA worded the variance in such a way that HUD would likely
 20 deny for lacking pertinent clarity. The bankruptcy court erroneously based its holding
 21 on the prejudicially biased HUD variance. Appellee's Brief at 11. The variance AHFA
 22 obtained from FHA, Dkt. No. 71-11, is misleading because it fails to define what
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1 income is excluded, whether the excluded income is Mr. Anzaldua's child support
2 payments or his entire income. As with every other communication from AHFA,
3 interpretation becomes a shell game where AHFA chooses only whatever
4 interpretation leads to foreclosure inspite the fact Ms. Tavares showed AHFA she had
5 a qualifying income. Doc. No. 3, Decl. of Monique Patzer, pg. 3, ¶11-16.
6

7 As for the partial claim, it again goes to AHFA denying the allegation without
8 proof. As calculated by her housing counselor, Ms. Tavares qualified for a
9 modification with a partial claim. Doc. No. 3, Decl. of Monique Patzer. Had AHFA
10 filed a claim there would be a certificate from HUD indicating the paid claim and in
11 some cases a transfer of title back to the beneficiary (HUD). Those funds would be
12 used to bring the borrower current and back into the loan. It is wholly unfair and
13 deceptive of AHFA to withhold filing a partial claim or participating in any available
14 default mitigation.
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17 Even though Ms. Tavares chose to ignore AHFA's discouragement of the use of
18 housing counselors, it remains an unfair or deceptive act because it has the capacity to
19 mislead other borrowers. Even when Ms. Tavares did not fire her housing counselor as
20 a result, the court should have acknowledged that while AHFA spent its time
21 discouraging the use of HUD approved housing counselors, it was not using its
22 opportunity with Ms. Tavares to properly assist her with mitigation she showed she
23 could afford. AHFA refused to review Ms. Tavares's application considering her true
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1 income which, pursuant the housing counselor, qualified Ms. Tavares for a loan
 2 modification. Moreover, AHFA's conduct is in direct conflict with clearly stated public
 3 policy under RCW 61.24.005.

4 **(2) occurring in trade or commerce**

5
 6 There is no dispute that the mortgage in question is included in the CPA's broad
 7 definition of the terms "trade" and "commerce" including "the sale of assets or
 8 services, and any commerce directly or indirectly affecting the people of the state of
 9 Washington." RCW 19.86.010(2).

10 **(3) affecting the public interest**

11
 12 The court erred in finding that AHFA's conduct did not have a public impact.
 13 Ms. Tavares sufficiently stated this element alleging AHFA's capacity to injure others
 14 RCW 19.86.093(2) & (3). As the District Court stated when restraining the non-
 15 judicial trustee sale of the subject property, "[T]o the extent that Defendant's practices
 16 undermine the purposes of Washington's Deeds of Trust Act (which include providing
 17 an efficient and inexpensive process and an adequate opportunity for borrowers to
 18 prevent wrongful foreclosure), they impact the public interest." *Tavares v. AHFA*, Dkt.
 19 No. 19, 2:17-cv-01599-MJP (U.S. Dist. Ct., Wash. Nov. 27, 2017). There is a decided
 20 public interest in protecting borrowers from prolonged and unnecessary foreclosures.
 21 As with above, Washington's Legislature declared that "[P]rolonged foreclosures
 22 contribute to the decline of the state's housing market, loss of property values, and
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1 other loss of revenue to the state....” RCW 61.24.005 Findings-Intent-2 001 c58 (1)(b).
 2 Common sense and the economic hardships of the last decade dictate that dilatory and
 3 manipulative lending practices have a significant public impact. *Syed v. Bank of*
 4 *America, N.A.*, 2:16-cv-01183-JCC, Dkt. No. 20, pg. 7, (U.S. Dist. Ct., W.D., Wash.,
 5 Nov. 22, 2016.)
 6

7 (4) injury to a person's business or property

8 The court erred in finding Ms. Tavares suffered no injury. On a motion to
 9 dismiss, the Court need not determine which of the parties’ positions is accurate. *Syed*
 10 *v. Bank of America*, 2:16-cv-01183-JCC, Dkt. No. 20. pg. 8, *citing Van Buskirk v.*
 11 *Cable News Network, Inc.*, 284 F.3d 977, 980 (9th Cir. 2002)(“Ordinarily, a court may
 12 look only at the face of the complaint to decide a motion to dismiss.”); *see also U.S.*
 13 *Bank Nat’l Assoc. v. Tait*, 2016 WL 5141990 at *2 (W.D. Wash. Sep. 21, 2016) (“At
 14 this stage of the litigation, the Court need not determine which of the parties’
 15 allegations are true as to what caused the Tait’s injury of an increased principal.”).
 16 Rather, courts ask whether the version of the facts alleged are plausible. Ms. Tavares’
 17 failure to pay cannot as a matter of law defeat causation. *Syed at* Dkt. No. 20. pg. 8. If
 18 anything, Ms. Tavares’ total deposits of over \$20,000.00 into the court registry is
 19 showing that the negative amortization since June 2016 is caused by AHFA’s
 20 mitigation failure rather than default. Negative amortization means the loan is
 21 becoming more expensive to modify due to the accrual of arrears while languishing in
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1 unmitigated default. *Frias v. Asset Foreclosure Servs., Inc.*, 181 Wash. 2d 412, 431-32,
 2 334 P.3d 529, 538. (2014), A plaintiff may be injured by conduct which causes
 3 increased principal and accrued interest. *U.S. Bank N.A. v. Tait*, 2016 U.S. Dist. LEXIS
 4 129046 (W.D.Wash. Sep. 21, 2016).

5 Here, the Second Amended Complaint alleges (SAC) Dkt. No. 69 of Adversary
 6 Proceeding alleges, “injury to property in the form of increased principal and accrued
 7 interest.” See SAC at Dkt. No. 69, pg. 13. The SAC specifically alleges, “AHFA's
 8 baseless refusal to review Ms. Tavares accurately and credibly ascertaining mitigation
 9 of her default with an affordable loan modification has injured her property by twenty-
 10 four months of needlessly accumulated debt.”

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 13 **(5) causation.**

14 The SAC alleges that, “[B]ut for ServiSolution's actions as alleged herein, the
 15 increased principal and accrued interest injury would not have occurred.”

16 As a direct and proximate result of its delay and needless obfuscation, AHFA caused
 17 the mortgage loan balance to increase and accrue arrears. In failing to address the
 18 issues of foreclosure, defendant AHFA created an outstanding principle balance far
 19 larger than it would have been had defendants simply complied with the law and
 20 mitigated the default. The SAC specifically pleads, “... had AHFA negotiated a loan
 21 modification shortly after June 2016, Ms. Tavares' loan principal would have
 22 decreased and be decreasing with each payment, and there would be no arrears.
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1 Interest would be accruing on a smaller principal with each passing month[.]...

2 AHFA's unfair and deceptive default mitigation practices added twenty-four months of
3 arrears, all of it avoidable.”

4 In sum, with regard to the sufficiency of the pleading, t he Court erred by
5 splitting up the alleged unfair and deceptive events and presuming the total sum effect
6 of AHFA’s conduct would not unnecessarily delay, confuse, and evade prompt useful
7 default mitigation in complete conflict with Legislative intent. *See* RCW 61.24.005
8 (Intent). It is mathematical that delay increases a defaulted loan’s cost (and decreases
9 the ability to mitigate as time progresses) by virtue of the accrual of arrears, interest,
10 and associated cost. Ms. Tavares alleges, and sufficiently showed, that but for AHFA’s
11 mitigation evasion, lack of a modification with a partial claim, Ms. Tavares would not
12 be suffering the increasing cost of her loan. Ms. Tavares agreed to release the
13 injunctive bond amount to be applied to the loan to decrease the loan injury and
14 increase the likelihood of an affordable modification.
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18 The fact there was no clear title was ultimately due to AFHA’s i ntransigence and
19 default mitigation evasion. AHFA foreclosed any opportunity to explore options for
20 releasing any junior liens.
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1 **2. It was error to deny leave to amend the adversary**
 2 **complaint.**

3 The Court erred by not granting leave to amend. FRCP 15 states, “The court
 4 should freely give leave when justice so requires.” Leave to amend should be granted
 5 even if no request to amend the pleading was made, unless the pleading could not
 6 possibly be cured by the allegation of other facts. *Ebner v. Fresh, Inc.*, 838 F.3d 958,
 7 968, (9th Cir. 2016). *See also Doe v. United States*, 58 F.3d 494, 497 (9th Cir.1995). The
 8 Ninth Circuit reviews district court denials for leave to amend *de novo* ensuring the
 9 “complaint would not be saved by any amendment.” *Carvalho v. Equifax Info. Svs.*,
 10 *LLC.*, 629 F.3d 876 (9th Cir. 2010).

11 Here justice requires that a minor who is a victim of the non-resident co-
 12 borrower’s sexual assault should not be uprooted and forced to relocate because the
 13 man who assaulted that minor refuses to cooperate and provide updated income data
 14 to AHFA. The exception is when the *facts* demonstrate futility. The law focuses on
 15 the facts and only permits dismissal when there could not possibly be other facts that
 16 once alleged, cure the insufficiency. Here the bankruptcy court ignored the housing
 17 counselor’s declaration and other facts to create a non-existent insufficiency. Leave to
 18 Amend substantively focuses on a factual basis for futility, it does not, as the
 19 bankruptcy court did, dismiss the case because the number of amendments reached
 20 some subjective level of impermissibility. Here, at least one previous amendment was
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1 administrative as this case originated in U.S. District Court, not in bankruptcy court.

2 This should not count against the Trustees under any FRCP 15 analysis. Nor should a
3 need for further amendment cause any prejudice as AHFA has not spent any time or
4 resources in discovery and it has received Ms. Tavares' cash outlay from the released
5 injunctive bond funds, no anticipated amendment would trigger any prejudice to
6 AHFA.
7

8 The claims Trustees allege in the Second Amended Complaint routinely survive
9 dismissal. It is the Appellant Trustee's position that the CPA claim is sufficiently pled
10 but further amendments could assist in accommodating the bankruptcy court's
11 position on sufficiency for stating a CPA claim. *See, Minie v. Selene Finance et*
12 *al*, 3:18-cv-5364RJB, (U.S. Dist. Ct., W.D. Wash. Mar. 22, 2019) (In circumstances
13 similar to the instant case, with respect to the CPA claims, the court in *Minie* held that
14 the defendants failed to meet their summary judgment burden. As here, the plaintiff in
15 *Minie* offered numerous specific facts supported by affidavits and declarations that
16 contradict facts offered by defendants.) See also, *Sergeant v. Bank of America et al*,
17 C17-5232BHS, (U.S. Dist. Ct., W.D. Wash. Sept. 6, 2017), *U.S. Bank Nat'l Assoc. v.*
18 *Tait*, 2016 WL 5141990 at *2 (W.D. Wash. Sep. 21, 2016), and *Johnson v. JP Morgan*
19 *Chase*, 14-5604RJB, (U.S. Dist. Ct., W.D. Wash. Aug. 11, 2015).
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24 The Appellant Trustees's could amend the complaint to address how mitigation
25 could have come prior to the expiration of the residential Mortgage Forgiveness Debt
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1 Relief Act of 2007 which expired in 2016 and its extension expired in 2017. The
2 amendment could update the tax consequences related to the effect debt cancellation
3 has on Trustees now, compared to what the tax impact would have been in 2016-2017.
4 Under the current tax regime, any tax obligation arising from any mortgage debt
5 cancellation is taxable. This could be significant as generally amounts removed from
6 the unpaid principal balance to make a modification affordable are added back to the
7 loan in the form of a balloon payment (often interest free) payable at term thus
8 avoiding the tax obligation a discharge would create. But, solving the tax problem
9 does not solve the increased cost issue. Where a more favorable loan modification was
10 available but for bad faith, the borrower may have suffered an injury to property
11 within the meaning of the CPA. *Frias v. Asset Foreclosure Servs., Inc.*, 181 Wash. 2d
12 412, 431-32, 334 P.3d 529, 538. (2014). A plaintiff may be injured by conduct which
13 causes increased principal and accrued interest. *U.S. Bank N.A. v. Tait*, 2016 U.S. Dist.
14 LEXIS 129046 (W.D.Wash. Sep. 21, 2016). A balloon payment consisting of arrears
15 accumulated by the lender's delay, which becomes payable upon sale of the property
16 or term of the Note is an undeniable injury to the borrower's business or property
17 because AHFA's delay adds an expense or cost that would not otherwise exist, and that
18 added cost ultimately decreases the investment value to the borrower because it
19 diminishes sale proceeds and looms as a likely unpayable debt if maturity occurs
20 before sale. Therefore the Trustee's complaint can be amended to clarify damages
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1 under recent tax reforms and the resulting impact those reforms have on mitigating the
2 mortgage default.

3 The complaint may also benefit from other updates. For example, Mr. Anzaldua
4 continues to refuse to cooperate with the modification application or any title transfer
5 process, confirming AHFA's role as a tool to retaliate against Ms. Tavares for having
6 taken court action to protect her child from further assault, while she had the income
7 to afford a modification. This lost opportunity to mitigate affordably is further injury
8 to property and business that can be claimed under the consumer protection act.
9

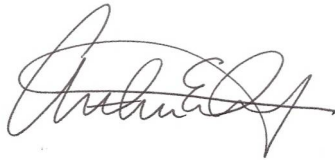
10
11 Consequently, AHFA's position also prevents Ms. Tavares from clearing title,
12 another condition to modification. Thus AHFA's refusal to cooperate creates the
13 situation that makes it impossible to avoid an unnecessary foreclosure and all the
14 while, Ms. Tavares could afford a loan modification. AHFA evaded doing a full review
15 of her income because the co-borrower's name, the man who molested her child, and
16 is subject to a state court NCO, remains on the defaulted mortgage.
17

18 VI. CONCLUSION

19
20 The Appellant bankruptcy trustees pray this Court reverse the bankruptcy
21 court's dismissal, and remand back to bankruptcy court with an order permitting
22 further proceedings to properly adjudicate the issues. The Second Amended
23 Complaint sufficiently states it claims and sufficient authority existed for AHFA to
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1 modify the loan for Ms. Tavares. This matter could have been resolved long ago had
2 AHFA simply acknowledged proven affordability and chosen to not evade mitigation.

3 Dated this 8th day of July, 2019.

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7 Arthur E. Ortiz, WSBA No. 26676
8 Attorney for Appellant Trustees
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VII. CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of FRBP 8015(a)(5) because the brief contains 3,264 words, excluding the parts of the brief exempted by FRBP 8015(g).

Dated July 8, 2019

s/ Arthur E. Ortiz
Arthur E. Ortiz, WSBA No. 26676
Attorney for Appellant Trustees

CERTIFICATE OF SERVICE

I hereby certify that on the 8th day of July, 2019, I caused to be electronically filed the foregoing APPELLANTS' REPLY BRIEF with the Clerk of the Court using the CM/ECF System which will send notification of such filing to the following:

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I declare the foregoing is true and correct.

DATED this 8th day of July, 2019 in Seattle, King County, Washington.



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